PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Item 9
Agenda ID 13927

ENERGY DIVISION **RESOLUTION G-3499 (Rev.1)**
June 11, 2015

R E S O L U T I O N

Resolution G-3499. Southern California Gas Company (SoCalGas) request for recovery of the Transmission Integrity Management Program (TIMP) Balancing Account balance as recorded on December 31, 2013.

PROPOSED OUTCOME:

- SoCalGas' request to recover its TIMP Balancing Account Balance as recorded at the end of 2013 is approved.
- SoCalGas shall allocate the under-collected TIMP balance using a functionalized method, not using an Equal Percent of Authorized Margin (EPAM) method.

SAFETY CONSIDERATIONS:

- SoCalGas' TIMP Balancing Account records pipeline integrity-related costs associated with federal regulatory requirements set forth in 49 CFR 192 Subpart O adopted following the passage of the Pipeline Safety Improvement Act of 2002.

ESTIMATED COST:

- $28,997,424

By Advice Letter 4632 filed April 11, 2014.

SUMMARY

D.13-05-010 authorized SoCalGas to establish a two-way balancing account to recover actual O&M expenses and capital expenditures of compliance with the Transmission Integrity Management Program (TIMP). SoCalGas filed Advice Letter 4632 requesting recovery of $28,997,424 for costs incurred for Years 2012 and 2013 in the TIMP Balancing Account and recorded as an

undercollection. This amount is in addition to the $28.6 million that the Commission authorized SoCal Gas to collect in D.13-05-010. The additional costs are primarily the result of additional requirements by PHMSA that were adopted after SoCalGas had prepared its cost estimates in 2010. SoCalGas' request to recover its TIMP Balancing Account Balance as recorded at the end of 2013 is approved.

SoCalGas' proposal to allocate the TIMP undercollection to customer classes using an EPAM method is denied. SoCalGas shall use a functionalized allocation to allocate the undercollection.

BACKGROUND

The SoCalGas Transmission Integrity Management Program (TIMP) was established as a result of the Pipeline Safety Improvement Act of 2002 and the enactment of 49 CFR Part 192 Subpart O (Subpart O).

Pursuant to Subpart O, operators of gas transmission pipelines are required to identify the threats to their pipelines in High Consequence Areas, analyze the risk posed by these threats, collect information about the physical condition of their pipelines, and take actions to address applicable threats and integrity concerns before pipeline failures occur.

Since the Pacific Gas and Electric Company (PG&E) pipeline rupture in San Bruno in September 2010, regulations such as "The Pipeline Safety, Regulatory Certainty, and Job Creation Act of 2011" have led the Pipeline and Hazard Materials Safety Administration (PHMSA) to change its reporting requirements and review existing transmission integrity requirements to identify areas for improvement.

In its 2012 GRC proceeding, Application (A.) 10-12-005, SoCalGas forecast $32.9 million for its TIMP-related Operations and Maintenance (O&M) expense for the test year. In D.13-05-010, the Commission authorized $28.6 million for Test Year 2012 which was $4.3 million or 13% lower than SoCalGas' request.

In Ordering Paragraph 19 of D.13-05-010, the Commission authorized SoCalGas to establish a two-way balancing account to recover actual TIMP compliance O&M expenses and capital expenditures.

Finding of Fact 202 states that any costs in excess of the authorized TIMP O&M costs and capital expenditures will be subject to recovery through a Tier 3 Advice Letter process. The TIMP balancing account is effective for the four-year GRC cycle ending December 31, 2015, or the effective date of SoCalGas' next GRC. Any over or under collected balance at the end of each year within the GRC cycle is to be carried over to the following year.

The TIMP Balancing Account was established in SoCalGas' tariff via Advice Letter (AL) 4507. The account became effective July 21, 2013. Although the TIMP Balancing Account only became effective on July 21, 2013, TIMP costs incurred as of January 1, 2012 are included in the account. D.13-05-010 adopted the effective date of January 1, 2012 for the change in the revenue requirement; accordingly, all regulatory accounts associated with the 2012 General Rate Case were also authorized with an effective date of January 1, 2012.[1]

With AL 4632, SoCalGas requests authority to recover an under-collection in the TIMP Balancing Account of $29.017 million (48% above the authorized revenue requirement) accumulated in 2012 and 2013. AL 4632 is the first advice letter to be submitted by SoCalGas by which it requests recovery of an under-collected TIMP Balancing Account balance.

SoCalGas proposes to amortize the TIMP balancing account amount in gas transportation rates on an Equal Percent of Authorized Margin (EPAM) basis.

NOTICE

Notice of AL 4632 was made by publication in the Commission's Daily Calendar. SoCalGas states that a copy of the Advice Letter was mailed and distributed in accordance with Section 3.14 of General Order 96-B.

[1] Assigned Commissioner and Administrative Law Judge's Scoping Memo and Ruling (March 2, 2012).

PROTESTS

Advice Letter (AL) 4632 was timely protested by the Office of Ratepayer Advocates (ORA), The Utility Reform Network (TURN) and the Southern California Generation Coalition. All three protests were filed on May 1, 2014.

ORA recommends that before a draft resolution is issued, the Energy Division verify and validate the reasonableness of the TIMP costs incurred by SoCalGas in excess of its authorized revenue requirement and audit the under-collection in the TIMP balancing account. ORA further recommends that the results of this audit and reasonableness review be described in detail within the draft resolution to support the Energy Division's recommendation.

TURN argues that SoCalGas did not provide enough evidence in the Advice Letter to establish the reasonableness of the recorded costs. TURN further recommends that the Commission should deny the requested relief in AL 4632 absent a demonstration that the recorded costs are indeed reasonable and necessary.

SCGC suggests that SoCalGas is improperly attempting to reverse D.13-05-010 by including the amount of TIMP costs that were reduced by the Commission in the GRC. SCGC also implies that it would have been more appropriate for SoCalGas to file an application for rehearing to contest the reduction in the amount of TIMP costs or to file a petition for modification to request the Commission reconsider the reduction. Secondly, SCGC argues that the AL does not contain sufficient detail to establish the reasonableness of the cost incurred. As such, SCGC recommends that SoCalGas Advice Letter 4632 be denied without prejudice.

SoCalGas filed a reply to the protests on May 8, 2014. SoCalGas argues in its reply that AL 4632 fully complies with D.13-05-010 and that SCGC's protest be rejected. SoCalGas also states that AL 4632 includes all of the expenditures incurred for TIMP activities, and asserts that SCGC's and TURN's claim that AL 4632 does not provide sufficient detail is unfounded. SoCalGas supports a review so long as such review does not result in additional delay.

DISCUSSION

The Energy Division reviewed 2012 and 2013 costs recorded in the TIMP Balancing Account and also examined some invoices on a selective, sampling basis. Aside from two minor cost items, the Energy Division found that the costs reviewed appeared to be appropriately recorded and incurred.

Aside from the minor adjustments, SoCalGas is authorized to recover the under-collected TIMP Balancing Account balance as of December 31, 2013**.**

D.13-05-010 adopted a two-way balancing account and advice letter process as an appropriate procedure for SoCalGas to recover TIMP-related O&M costs and capital expenditures of complying with 49 CFR 192 Subpart O.

D.13-05-010 (Section 9.3.3.2.2.2.3, p. 421) states:

> ... In accordance with Pub. Util. Code § 969, we adopt a two-way balancing account to recover the TIMP-related O&M costs and capital expenditures of complying with Subpart O. However, this balancing account shall be subject to the following. Any costs in excess of the O&M costs and capital expenditures authorized for these TIMP costs shall be subject to recovery through a Tier 3 advice letter process. Such a restriction on this two-way balancing account will ensure that the TIMP-related costs are reasonable and necessary. We will also allow the year-end balance in that two-way balancing account to be carried forward into the following year. A two-way balancing account is appropriate due to the costs of complying with Subpart O and possible changes in pipeline inspection requirements in the future. A two-way balancing account will also ensure that SoCalGas has sufficient funds to carry out all necessary TIMP-related work to ensure that its gas transmission system remains safe and reliable, while the AL process will ensure that costs in excess of what has been authorized will be subject to review.

Furthermore, D.13-05-010 Finding of Fact 202 states:

> A two-way balancing account for SoCalGas to recover the costs of complying with TIMP is appropriate due to the cost of compliance, and possible changes in pipeline inspection requirements in the future, and any costs in excess of the authorized TIMP O&M costs and capital expenditures will be subject to recovery through a Tier 3 AL process.

Use of the advice letter process by SoCalGas to request recovery is in accordance with the guidance in D.13-05-010 for recovery of additional O&M costs and capital expenditures.

Accordingly, SCGC's suggestion that SoCalGas' Advice Letter request as improper is incorrect.

In addition, D.13-05-010 goes on to state in Finding of Fact 204:

> Parties will have the opportunity to review the reasonableness of these TIMP-related expenses in SoCalGas’ balancing account when those expenses are reported in the Annual Regulatory Account Balance Update, or in the Tier 3 AL filing.

Protestants have not conducted their own review of SoCalGas' TIMP costs.

None of the three protestants have submitted requests for additional information from SoCalGas to pursue further review of the TIMP O&M costs and capital expenditures. In its protest, ORA states that due to resource constraints, ORA did not intend to audit the TIMP balancing account, but supports a detailed review by Energy Division. In its reply to the protests, SoCalGas agreed that a review by Energy Division aligns with the advice letter process established in D.13-05-010. SoCalGas also agreed to provide additional information to both TURN and SCGC to allow parties to conduct an independent review. According to SoCalGas, none of the protestants requested additional information.

The Energy Division staff has reviewed the 2012 and 2013 TIMP O&M costs and capital expenditures included in the TIMP balancing account. Energy Division also conducted an invoice level review of some costs for verification using selective sampling.

In response to Energy Division staff data requests, SoCalGas provided Energy Division with additional supporting information extending to the invoice level to demonstrate that the reviewed costs and expenditures were appropriately incurred TIMP-related expenditures.

For verification at the invoice level, Energy Division staff examined TIMP O&M expenses and capital expenditures selecting three sample months during Year 2012 and 2013: June 2012, December 2012 and December 2013. These three months were selected for review because June is typically a high construction month and December being year-end close-out.

Of the several hundred entries in the utility ledger recorded during those months, staff selectively identified a number of line items based on anomalies in the description or the amount logged. Each ledger item in turn contained several cost elements. Of these cost elements, staff again selectively identified a number of cost elements to request invoices from the utility. SoCalGas provided over fifty invoices associated with the cost elements. Staff review included both O&M expenses and capital expenditures.

Energy Division staff found that the expenses and expenditures that it examined appeared to be appropriately recorded to the TIMP Balancing Account and appeared to be reasonably incurred. As a result of the data requests and staff review, SoCalGas made two adjustments to the balancing account amounting to a reduction of $19,433 to the under-collection.

The TIMP Balancing Account under-collection is summarized in the table below:

TIMP Balancing Account Revenue Requirements Year 2012-2013 ($000):					
	Actual/Projected	Authorized[2]	Undercollection	Interest	TIMP Balancing Account
O&M	86,049	57,982	28,067		28,067
Capital-Related Rev Req	2,775	1,921	854		854
Cost of Capital Adjust.	-	(52)	52		52
Interest				24	24
Total	88,824	59,851	28,973	24	28,997

The additional costs requested for recovery are primarily due to additional TIMP O&M expenses.

SoCalGas states that there are three primary reasons why the TIMP Balancing Account had a substantial under-collected balance at the end of 2013. First, the amount authorized by the Commission was below SoCalGas' forecast. This accounts for $8.7 million of the under-collection. Second, SoCalGas "did not foresee conditions that ultimately led to increased TIMP-related costs." This accounts for $19.4 million of the under-collection. And third, "as a result of how capital expenditures are recovered and balanced," SoCalGas has recovered $1 million less than the amount needed to fully recover the revenue requirement associated with capital expenditures.

SoCalGas states that part of the under-collection occurred because several activities were forecast to have no spending in Test Year 2012, but some costs were actually incurred. These forecasts were done prior to the adoption of incremental regulatory requirements that drove work in these categories. Additional costs were driven by supplementary assessments, program management and support costs, pipe sampling, cathodic protection survey, and completion of feature studies. In addition, SoCalGas states that some projects that were initially contemplated to begin in 2013 were accelerated and initiated in 2012.

[2] 2013 authorized O&M and capital-related revenue requirement increased by the 2.65% attrition adjustment adopted in D.13-05-010.

TIMP O&M expenses exceeded authorized amounts by $28 million. Capital expenditures were also more than forecast, by $7.7 million. The TIMP Balancing account records the revenue requirement associated with these capital expenditures. That revenue requirement is comprised of return on ratebase, taxes on return, depreciation and ad valorem tax. The annual revenue requirement on capital expenditures is typically much less than the capital expenditure itself. Thus, the under-collection in the TIMP at year-end 2013 ($854,000) due to capital expenditure is much less than $7.7 million. [3] But this revenue requirement will occur over a longer period (the life of the capital asset), and will steadily increase as capital expenditures are added.

The Pipeline Safety, Regulatory Certainty, and Job Creation Act of 2011 led PHMSA to change reporting requirements. As a result, PHMSA implemented new data collection and Maximum Allowable Operating Pressure (MAOP) validation regulations.

SoCalGas states that the 2012 GRC application was prepared in early 2010 prior to the implementation of regulations resulting from the San Bruno pipeline rupture. Changes such as "The Pipeline Safety, Regulatory Certainty, and Job Creation Act of 2011" led PHMSA to change reporting requirements and review the existing transmission integrity requirements to identify areas for improvement. The new legislation incorporated provisions such as: requiring the installation of automatic or remote-controlled shut-off valves on new transmission pipelines; requiring gas transmission pipelines operators to verify records and confirm maximum allowable operating pressure; and reauthorizing and strengthening the authority of the PHMSA.

SoCalGas asserts that in 2010, when it was preparing its GRC estimates, it did not yet have a complete history of the cost of repairs or remediations that would be driven by those baseline assessment findings and did not yet have experience with addressing certain issues that arose when conducting assessment and remediations in sensitive areas.

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[3] In addition, as SoCalGas noted in Al 4632, certain ratemaking anomalies arise when recording capital-related revenue requirement in a balancing account, and this can cause an under-collection not primarily related to differences between actual and authorized levels.

On August 25, 2011, PHMSA published an Advance Notice of Proposed Rulemaking (ANPRM) for enhanced integrity management and other pipeline safety regulations for gas transmission pipelines. The ANPRM addressed current industry practices, the effects of enhanced regulations on safety and cost, and the best method to implement proposed regulations.

As a result, PHMSA implemented new data collection and Maximum Allowable Operating Pressure (MAOP) validation regulations. To comply with these new MAOP reporting regulations, SoCalGas states that its data collection required new formatting and additional data collection on non-High Consequence Area (HCA) pipelines for MAOP validation. In addition, SoCalGas states that it has proactively expanded and accelerated its Integrity Management Program in anticipation of new regulations as discussed in PHMSA workshops, such as retrofitting pipelines for in-line inspection and assessment allowing for improved and quicker MAOP validations.

California Assembly Bill 56 and Senate Bill (SB) 879[4] adopted additional TIMP related regulations in 2011.

Codified as Public Utilities Code section 969, the passage of the bills required extensive safety reporting requirements and records as well as the establishment and maintenance of a balancing account for the recovery of expenses related to the gas corporation's transmission pipeline integrity management program established pursuant to Subpart O.[5]

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[4] Senate Bill 879 added Section 969 to the Public Utilities Code.

[5] Public Utilities Code section 969. In any ratemaking proceeding in which the commission authorizes a gas corporation to recover expenses for the gas corporation's transmission pipeline integrity management program established pursuant to Subpart O (commencing with Section 192.901) of Part 192 of Title 49 of the United States Code or related capital expenditures for the maintenance and repair of transmission pipelines, the commission shall require the gas corporation to establish and maintain a balancing account for the recovery of those expenses. Any unspent moneys in the balancing account in the form of an accumulated account balance at the end of each rate case cycle, plus interest, shall be returned to ratepayers through a true-up filing. Nothing in this section is intended to interfere with the commission's discretion to establish a two-way balancing account.

SoCalGas also notes in AL 4632 that pipeline operators were not required to complete all their first or "baseline" pipeline assessment under Subpart O until 2012.

In response to Energy Division data requests, SoCalGas has provided several examples where forecasted costs and expenditures associated with a specific project encountered additional assessments and remediation causing actual costs to be higher than initially forecasted.

Cost overruns were generally caused by additional work required during construction after the initial inspection and estimate was forecasted, such as additional permitting and environmental work required by other regulatory agencies, accidental equipment failures, additional pipeline anomalies and additional cleaning runs of pipelines.

The Safety and Enforcement Division (SED) is in the process of conducting the second of a two part inspection that consists of records review, validation of the SoCalGas TIMP implementation records and field verification.

In the course of its audit, SED is examining the overall management of the TIMP, as well as SoCalGas TIMP practices. SED's records review is near completion and the validation review of the SoCalGas TIMP implementation records and field verification is scheduled for completion by the end of 2015. The Commission may need to revisit the financial costs and expenditures associated with potential issues resulting from SED's review and audit.

We find that the new PHMSA regulations and Senate Bill 879 did require SoCalGas to undertake activities in addition to what SoCalGas had forecasted at the time it was preparing for its 2012 GRC (A. 10-12-005). As the Energy Division staff found no inappropriately recorded or unreasonably incurred costs in its invoice level review of selected samples, the additional TIMP O&M expenses and capital expenditures incurred by SoCalGas for years 2012 and 2013 should be approved.

SoCalGas should ensure that the forecasts of TIMP costs in its Test Year 2016 GRC application accurately reflect the costs that it will need to incur. Variations between forecasted costs and actual costs should be minimal so these costs do not have to be addressed outside of the GRC proceeding.

We reject SoCalGas' proposal that the undercollection be allocated among customers based on the Equal Percent of Authorized Margin (EPAM). The under-collection of the TIMP Balancing Account shall be allocated based on the functionalized allocation of transmission-related costs as provided in SoCalGas' most recent Triennial Cost Allocation Proceeding (TCAP) decision. SoCalGas shall submit a supplement advice letter to AL 4632 to set forth rate impacts using the functionalized allocation.

Under the EPAM method, a very large percentage of the TIMP under-collection would be allocated to core gas customers. According to Attachment B of AL 4632, core customers would be allocated 93% of the undercollection using the EPAM method. This result occurs mainly because a large proportion of SoCalGas revenue requirements are allocated to core gas customers, due to the large allocation of customer-related and distribution costs. Customer-related costs and distribution costs are the largest portion of SoCalGas' base margin. Transmission-related costs are allocated to core customers in much smaller percentages.

Although D.13-05-010 adopted the TIMP Balancing Account, it did not specify the allocation method for the SoCalGas TIMP Balancing Account under-collection. However, in D.14-06-007, the Commission addressed proposed cost allocation methods for the SoCalGas/SDG&E Pipeline Safety Enhancement Plan. There, the Commission noted that two different methods were suggested for allocating pipeline safety enhancement costs: (1) a "functionalized approach" where the costs are allocated to a particular component of gas service and then in turn finally allocated to different customer class based on that class's use of each particular component of service; and (2) the EPAM method based on the notion that the PSEP was fundamentally different from TIMP. D.14-06-007 specifically states: "any Safety Enhancement costs that are functionalized as backbone transmission costs are to be allocated to the Backbone Transmission Service customer class consistent with the allocation of the existing rate design." The Commission rejected the use of the EPAM method, and determined that the "cost of these new facilities should be allocated in the same manner as the old facilities were allocated."[6]

[6] D. 14-06-007, Section 9: Allocating Safety Enhancement Costs.

Furthermore, in D.12-12-030, the Commission addressed the appropriate allocation methodology for PG&E's gas transmission safety costs incurred under its Pipeline Safety Enhancement Plan (PSEP). In that decision, the Commission adopted an allocation of PSEP costs to customers based on their annual percentages of transmission-related revenue requirements.[7]

The functionalized allocation of the TIMP under-collection is consistent with D.14-06-007 and D.12-12-030, while the EPAM is not. SoCalGas shall submit a supplemental advice letter to set forth rates based on the functionalized allocation method.

COMMENTS

Public Utilities Code section 311(g)(1) provides that this resolution must be served on all parties and subject to at least 30 days public review and comment prior to a vote of the Commission. Section 311(g)(2) provides that this 30-day period may be reduced or waived upon the stipulation of all parties in the proceeding.

The 30-day comment period for the draft of this resolution was neither waived nor reduced. Accordingly, this draft resolution was mailed to parties for comments on April 21, 2015.

SoCalGas filed timely comments on June 1, 2015. SoCalGas noted that the draft resolution neglected to address the period over which the TIMPBA undercollection should be recovered. Additionally, SoCalGas stated that, due to the integrated nature of their transmission systems and rate recover mechanisms, SDG&E should also be directed to file a Tier 2 Advice Letter to set forth gas rates to recover their allocation of TIMPBA costs. Finally, SoCalGas mentioned that SoCalGas and SDG&E should be authorized to file a Tier 1 Advice Letter to remove the authorized TIMPBA amortization at the end of the twelve month recovery period. This resolution has been modified to reflect SoCalGas' concerns.

[7] D.12-12-030, Section 5.2.6: Cost Allocation and Rate Design

FINDINGS

1. SoCalGas filed AL 4632 on April 11, 2014 to request recovery of the under-collected TIMP Balancing Account balance of $29.017 million for years 2012 and 2013.
2. The costs included in the TIMP Balancing Account are incurred in response to the mandated federal pipeline safety regulations including, but not limited to requirements associated with Subpart O, Gas Transmission Pipeline Integrity Management.
3. The TIMP Balancing Account was authorized by Commission Decision 13-05-010.
4. Ordering Paragraph 19 of D.13-05-010 authorized SoCalGas to establish a two-way balancing account to recover the TIMP O&M costs and capital expenditures of complying with Subpart O.
5. D.13-05-010 states that any costs in excess of the authorized TIMP O&M costs and capital expenditures will be subject to recovery through a Tier 3 Advice Letter process.
6. None of the three protestants submitted requests for additional information from SoCalGas to pursue further review of the TIMP O&M costs and capital expenditures.
7. SoCalGas' 2012 GRC Application 10-12-005 was prepared prior to certain changes in reporting requirements by PHMSA.
8. Changes in pipeline safety regulation increased SoCalGas' actual TIMP costs and expenditures, and were among the reasons why TIMP costs were higher than initially forecasted.
9. Energy Division conducted an invoice level review based on a sampling of the TIMP O&M costs and capital expenditures included in the TIMP Balancing Account requested in AL 4232.
10. As a result of Energy Division's review, SoCalGas made two adjustments to the balancing account amounting to a reduction of $19,433 to the undercollection.
11. SoCalGas should be allowed to recover the TIMP Balancing Account undercollection of $28,997,424.
12. The EPAM method is inconsistent with the allocation of transmission pipeline safety costs recognized in recent CPUC decisions.

13. SoCalGas' proposal to use the EPAM method to allocate the under-collection should be denied.
14. SoCalGas should use a functionalized method to allocate the TIMP Balancing Account under-collection.

THEREFORE IT IS ORDERED THAT:

1. Southern California Gas Company request to recover its Transmission Integrity Management Program Balancing Account Balance as recorded at the end of 2013 for Years 2012 and 2013 is approved, as modified by a minor adjustment.
2. Southern California Gas Company is authorized to recover from ratepayers the under-collection of $28,997,424 over the twelve month period beginning the month following the approval of the supplemental advice letter required by this resolution in Ordering Paragraph 3.
3. Within 20 days of the date of this resolution, Southern California Gas Company shall file a supplemental Tier 2 Advice Letter to set forth gas rates to recover the Transmission Integrity Management Program Balancing Account under-collection based on a functionalized allocation method.
4. Within 20 days of the date of this resolution, San Diego Gas & Electric Company shall file a Tier 2 Advice Letter to set forth gas rates to recover its allocation of the authorized Transmission Integrity Management Program Balancing Account Balance over the twelve month period beginning the month following approval of the supplemental advice letter required by this resolution in Ordering Paragraph 3.
5. If the conclusion of the twelve month recovery period does not coincide with another rate change, Southern California Gas Company and San Diego Gas & Electric shall each file a Tier 1 Advice Letter to remove the authorized Transmission Integrity Management Program Balancing Account Balance.

This Resolution is effective today.

I certify that the foregoing resolution was duly introduced, passed and adopted at a conference of the Public Utilities Commission of the State of California held on June 11, 2015; the following Commissioners voting favorably thereon:

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TIMOTHY J. SULLIVAN
Executive Director